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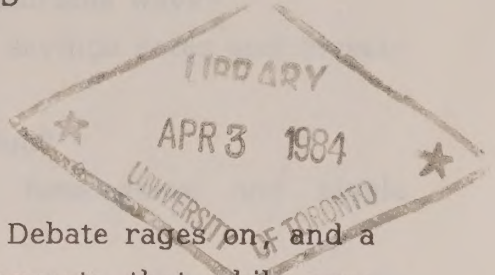
NEWS RELEASE #1: PENSIONS TODAY AND TOMORROW
BACKGROUND STUDIES

A GENERAL OVERVIEW OF THE ISSUES

TORONTO ... The Great Canadian Pension Debate rages on, and a study by the Ontario Economic Council suggests that while some problems need immediate attention, there are no fast and easy answers to the questions raised by the debate over pension reform. The study indicates pensions and pension reform will be a subject that will no doubt maintain a significant position in public policy debates for years, to come.

This study, *Pensions Today and Tomorrow: Background Studies*, offers an in-depth analysis of pensions and an evaluation of the various pension reform proposals that have surfaced in the current debate. It points out that a complex system of programs exists in Canada to ensure adequate material provision for the elderly, but there is some concern that the system as a whole is in some respects inefficient and inequitable. Moreover, the proportion of the population that is elderly and non-working, and therefore drawing benefits, is expected to increase significantly for demographic reasons. The result has been a growing belief in many areas in the potential and need of pension reform. Owing to the complexity of the overall old age security system, the issues raised affect all aspects of our economic life and often lead to controversial proposals.

The contents of this study throw light on the most important issues, such as:





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The contents of this study throw light on the most important issues, such as:

- To what extent should one generation support another?
- Do federal/provincial rivalries interfere with the pension structure?
- Will reform proposals interact in undesirable ways?
- How do pension contributions affect savings rates and investment patterns?
- Should pensions be indexed to inflation?
- Does the present system neglect homemakers and single women?
- Should government play a greater or smaller role in the future?

The first three papers in this volume provide an overview of the pension reform issues.

Adil Sayeed, a researcher with the Council, summarizes and compares the positions advocated by ten different organizations - some of which represent private business and labour interests and some of which were appointed by governments to develop reform recommendations. Sayeed quotes directly from their reports, to indicate the variety of recommendations that have been presented to the Canadian public. The proposals are divided into two groups: those dealing with public pensions and those dealing with private pensions. Throughout his paper, Sayeed's purpose is to clarify the differences of opinion among these organizations and to indicate areas of agreement.

A key area of Sayeed's overview involves transfer payments and the differences affecting the single elderly and the married elderly.

'The combined total of Old Age Security (OAS), Guaranteed Income Supplement (GIS), Guaranteed Annual Income Supplement (GAINS), and Ontario tax grant payments to a single elderly resident of

Ontario with no other income was \$6,870.50 in 1982. This amount is 23 per cent below Statistics Canada's low-income cut-off level of \$8,914 for a single person living in a metropolitan area. Combined total payments to a married couple with no other income amounted to \$12,543.70 in 1982, or 7 per cent above the low-income cut-off level of \$11,761 for a two-person household. According to the most recent estimates available from Statistics Canada, 45 per cent of the 65-and-over population in 1980 was unmarried. Of the single elderly, 76 per cent were women. Of unattached senior citizens living alone, 61.5 per cent were living on incomes below the low-income cut-off, compared to 14.2 per cent of those senior citizens living with others.'

In a later chapter, Adil Sayeed analyses the current arrangements for tax-transfer benefits for the elderly. He concludes that income support for single citizens is 'clearly inadequate when compared to the assistance granted to married couples'. Sayeed's calculations reveal our present system's generosity to the wealthy and lead to proposals that would shift benefits from the wealthy to those most in need. For example, our current income tax system provides special old-age exemptions and pension deductions which benefit the rich much more than the poor. These could be eliminated, with income tax so generated being transferred to the poor. Alternatively, they could be replaced with a refundable, income-tested tax credit.

Colleen Hamilton, a Research Associate, and John Whalley, a professor, both with the Department of Economics, University of Western Ontario discuss proposals to reform public pensions. In particular, they focus on the proposals of the federal government's Green Paper.

Their introduction summarizes their criticisms of the Green Paper: that in the public pension area, it focuses exclusively on expansion of Canada Pension Plan (CPP) benefits, ignoring the fact that the majority of public sector income support for the elderly occurs primarily through Old Age Security (OAS) and Guaranteed Income

Supplement (GIS), not the CPP; that it ignores the issue of whether such support programs should be shifted from universal coverage to higher payments aimed specifically at those most in need; that it fails to examine program interaction, through which increases in the CPP may be offset by automatic decreases in GIS and provincial income-supplement programs; that it does not adequately consider demographic impacts on pensions, particularly the financial difficulties that will arise due to the shifts in the population age structure; that it does not examine the alternatives between raising contributions or reducing benefits; that it does not discuss the constitutional role of the provinces in pension reform; and that it fails to consider many of the proposals that could improve pension arrangements in Canada.

Hamilton and Whalley emphasize that 'The nature of the political process is that future generations will have to consent to benefits paid to today's workers when they retire, and will have the political power to change benefits if they so wish'.

They note that shifts in the population's age structure will inevitably result in intergenerational transfers through which some people will gain while others lose. They comment on the relationships between pension arrangements and other economic factors, such as the nation's savings rate, the willingness of people to work, and the age at which people decide to retire.

'A further issue in pension reform not raised in the Green Paper, but central to the debate on social security in the U.S., is whether we should think about raising the retirement age. Even a small change in the retirement age above 65 would have substantial impacts on the budget situation, both for the CPP and for OAS-GIS. If average life expectancy conditional on reaching age 20 (entry to the labour force) were age 75 averaged over males and females, then raising the qualifying age to 66 would save annually approximately \$1 billion at current expenditure levels; and to about age 67, \$2 billion. Such a change could sharply reduce the

pressures on contributions and taxes from any future funding crisis.'

Poverty among the current elderly receives special attention, and the authors examine the degree to which the elderly rely on various income sources, including pension programs. They illustrate the levels of income support payments to different categories of recipients. This information is then compared with poverty-line estimates.

Hamilton and Whalley also examine population projections to calculate the impact of probable demographic changes on public pension funding. They consider the issues of special concern to women. And they describe provincial rights in the reform process, including the opportunity to borrow from the national CPP fund.

Finally, Hamilton and Whalley present their own preferred reforms. They recommend that benefits be restructured rather than expanded, since they believe that current benefit levels are adequate and that the problems with our system lie in specific, easily defined areas. In particular they favour a shift of Old Age Security (OAS) from our universal basis to a new income-tested basis. They point out that this would allow substantial sums of money to be reallocated.

'Unpublished data from Statistics Canada's Survey of Consumer Finance indicate that in 1981, 12.8 per cent of OAS payments went to families with incomes greater than \$30,000; 23.9 per cent went to those with incomes greater than \$20,000; and 49.8 per cent went to families with incomes in excess of \$11,000. Total expenditures on OAS in 1981 were \$5.3 billion. Thus an income limit of \$30,000 would have saved approximately \$0.6 billion in 1981; a limit of \$20,000 approximately \$1.2 billion; and a limit of \$11,000 approximately \$2.6 billion. Even the \$30,000 limit would more than finance the Green Paper proposals since \$0.5 billion was around 20 to 25 per cent of CPP benefits paid, and the contribution rate increases projected from the Green Paper proposals are con-

siderably less than 20 per cent. Thus, as a method of allowing better targeting of income support to those most in need, this approach has a lot to commend it. As a result it has received the endorsement of several groups examining the pension reform issue in recent years.'

They conclude that a much wider range of options exists for Canadians in approaching public pension reform than are laid out in the Green Paper. They say the 'big' issues in public pension reform are not fully dealt with in the Green Paper. They believe that both the importance of the issues and their key role in Canadian economic policy will preoccupy policymakers for the next few decades. Rather than concluding a policy debate, the Green Paper may well prove to be a prelude to an expanding debate.

James Pesando, a professor, Department of Economics, University of Toronto, and Research Associate, National Bureau of Economic Research, has analysed the Green Paper proposals for the reform of employer-sponsored pension plans. He begins with an examination of 'the two major... reasons why firms provide defined-benefit plans for their employees.

The first is that pensions represent a tax-favoured vehicle for saving ... The second... is that these plans may play a central role in incentive-oriented, long-term labour contracts'. Since labour turnover imposes employer costs, firms have not been eager to facilitate pension portability. Furthermore, if earlier vesting is legislated, then firms may adopt alternative approaches to reduce labour turnover such as steeper wage grids, and they may reduce employer investment in the knowledge and skills of employees.

Pesando discusses the incidence of pension costs, noting that the worker 'bears the cost of improved pension benefits... via reduced current wages or other concessions in the total compensation package'. An exception occurs when legislated improvements are made retroactive, a situation which he describes as 'bad public policy'.

He notes that many workers prefer not to participate in private plans. He emphasizes that many reform proposals are based on an 'outright paternalism' which believes that 'if left to their own discretion, workers may make inappropriate consumption-saving decisions and thus allocate too little of their lifetime earnings to provide for their consumption needs during retirement'. The fact that some workers lack secure pension arrangements is not necessarily unfair as the Green Paper suggests, but rather may reflect the conscious decisions of workers to opt for other forms of compensation.

A major portion of Pesando's report is devoted to the issue of inflation protection. Here he reviews academic literature and then turns to a technical discussion of the mechanics for instituting inflation protection through various 'excess earnings' provisions.

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Pensions Today and Tomorrow: Background Studies, 486 pages, price \$9.00, is available at the following outlets:

The Ontario Government Bookstore, 880 Bay Street, Toronto, 965-3088 to those shopping in person. Out-of-town customers may write: Publications Section, Fifth Floor, 880 Bay Street, Toronto, Ontario, M7A 1N8, or telephone 965-6015 (toll-free long distance, 1-800-268-7540; in northwestern Ontario, 0-Zenith 67200). A cheque or money order, payable to the Treasurer of Ontario, must accompany all mail orders.

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